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SUBJECT: SCENE SETTER: POTUS NOVEMBER 6-7 VISIT TO PANAMA

1. (U) This message is sensitive but unclassified. Please protect accordingly.

2. (SBU) Embassy Panama extends its warmest welcome to President Bush for his upcoming visit to Panama. Canal expansion, bilateral security cooperation, and good governance initiatives currently top the bilateral agenda.

3. (SBU) President Bush's November 6-7 visit to Panama, as the government of President Martin Torrijos enters its fifteenth month, signals the interest of both countries in strengthening their already excellent relations. Elected as a modernizing, anti-corruption reformer by the largest post-1989 plurality on record (47% of the vote and 41 out of 78 legislative seats), Torrijos has made clear that his most important foreign policy priority is relations with the United States. He also has acted to deepen our two-countries' mutual focus on counter-terrorism capabilities, combating international criminal networks, and expanding trade and investment. A USG inter-agency delegation visited Panama September 28-30 to discuss U.S.-Panama cooperation on Panama's Secure Trade and Transportation Initiative (PST & TI), a proposal to re-structure and improve Panama's security infrastructure.

#### Canal Expansion

4. (SBU) The Torrijos team has made Canal expansion a top priority. The proposed Canal expansion project to construct a third set of locks could cost \$8 billion and take 8-10 years to complete. The GOP expects the project will be a transforming event for Panama that will provide jobs and set the tone economically for years to come. Given growing trade between East Asia and the U.S. eastern seaboard the expansion is central to maintaining the Canal's future viability and is expected to be financed through a combination of Canal revenues, new user fees, and bridge loans. However, Panama's constitution requires a national referendum to approve the idea. This referendum could occur in 2006 or 2007. A September 2005 CID-Gallup poll showed that a majority of Panamanians would vote in favor of Canal expansion.

#### Canal Stewardship

5. (SBU) During the past five years, the Panama Canal Authority (ACP) has proven itself an able administrator, turning the Panama Canal into an efficient and profitable business. Since the 1999 hand over, the ACP has reduced average Canal transit times, has reduced accidents in Canal waters, and has overseen large-scale upgrade and maintenance projects. The ACP also has increased revenues, which in FY 2004, exceeded \$1 billion for the first time and contributed \$332 million to the GOP budget.

#### GOP Priorities

6. (SBU) The Torrijos government's principal priorities are economic development, job creation, poverty alleviation, investment, fiscal reform, and government transparency. Torrijos has faced large challenges from the outset: a serious budget shortfall; a near-bankrupt national retirement and medical system (the Social Security Fund); and faltering public confidence in government institutions and the rule of law. Pressures from well-entrenched interest groups have frustrated the Torrijos administration's reform plans. Torrijos has worked to complete Free Trade Agreement (FTA) negotiations with the United States, and launch a more activist and "coherent" foreign policy (including closer relations with Western Europe). After a "review" of Panama's relations with Taiwan and China, the GOP has decided to stick with Taiwan.

#### President Torrijos and a New Generation

7. (SBU) Torrijos has surrounded himself with young, primarily U.S.-educated professionals like himself, and has marginalized "old guard" supporters of former President Ernesto Perez Balladares (1994-99). He has appointed many pro-U.S. technocrats to his cabinet, although they lack experience. Most of the cabinet are respected professionals without excessive baggage from Panama's 21-year military

dictatorship or the PRD's anti-U.S. faction.

#### Poverty: Chief Structural Issue

18. (U) At \$4500, Panama's per capita GDP is Latin America's third highest (following Mexico and Chile). However, Panama's solid GDP growth in recent years (6.2% in 2004, about 5.7% so far in 2005) and pursuit of trade liberalization have yet to translate into broadly shared prosperity. Panama faces the second-worst income distribution pattern in Latin America, persistent poverty (40% overall, higher than 90% in some rural areas), and stubbornly high unemployment (officially about 12%, with 20-25% underemployment). Moreover, Panama's dollarized economy currently faces the highest rate of inflation (about 3%) the country has seen in the past 23 years, as rising fuel and food prices place greater hardship on low-income Panamanians.

#### Free Trade Agreement

19. (SBU) Negotiations on a bilateral Free Trade Agreement (FTA) began in April 2004 under President Moscoso. To date, eight negotiating rounds (the last one in February 2005) have failed to produce an agreement, mainly due to Panamanian sensitivities in agriculture, such as rice, poultry, and pork. Panama also wants to increase its sugar quota. The Torrijos administration views a bilateral FTA as imperative to attract investment, increase exports, and make Panama competitive with the CAFTA countries. USTR and GOP negotiators are discussing next steps.

#### Security and Law Enforcement Policy

10. (SBU) The Torrijos government is highly focused on Canal and maritime security and combating terrorism and transnational crime, although it has not yet found the resources to adequately patrol Panama's long Caribbean and Atlantic coastlines and to secure Panama's porous border with Colombia against guerrilla infiltration. U.S.-Panamanian cooperation in law enforcement and security has steadily improved in recent years. That has led to increasing narcotics seizures, better investigations, active maritime law enforcement, more specialized units, and better detection of money laundering and illicit financial flows. While the USG-GOP relationship is good, Panama's law enforcement institutions are weak and suffer from limited resources and professionalism. On May 12, 2004, the U.S. and Panama signed a Proliferation Security Initiative (PSI) Shipboarding Agreement. Panama gave early political support to the Coalition of the Willing and ratified a bilateral Article 98 Agreement.

#### Security Cooperation

11. (SBU) The GOP recognizes that securing the Canal and Panama's borders requires a mature, collaborative bilateral relationship. Panamanians now are eager to accept mil-to-mil security training and equipment, as was shown during the August 2004 and August 2005 multinational PANAMAX naval exercises that centered on Canal defense. PANAMAX 2005 counted 15 participating nations. The GOP has welcomed an increased number of USG-sponsored Medical Readiness Exercises and other DOD rural humanitarian programs, which construct schools and clinics, and highlight the U.S. military's humanitarian side. New Horizons 2005, in the Azuero Peninsula, received wide and favorable press coverage.

#### Our Third Border

12. (SBU) The Canal remains an attractive and vulnerable terrorist target, although good Panamanian defense planning and U.S. training and equipment have made any potential terrorist attack more difficult. To protect water resources, the Panama Canal Authority (ACP) has committed to match dollar-for-dollar AID's three-year \$2.5 million integrated watershed management program. Despite significant progress, Panama continues to be an important transit point for drug smugglers, money launderers, illicit arms merchants, and undocumented immigrants heading north.

#### Maritime Security

13. (SBU) The GOP is acting to end abuses in Panama's open ship registry and mariner identification documents. Panama's ship registry, the world's largest, comprises one-quarter of the world's ocean-going fleet (5,525 large commercial vessels). About 13% of the U.S. ocean-going cargo transits the Canal each year. Panama's seafarer registry currently licenses over 264,000 crew members. Port services grew dramatically from about 200,000 containers per year in the early 1990s to 2 million by 2003. Panama now boasts the leading complex of port facilities in Latin America. In response to our homeland security concerns, the new GOP is working to greatly improve security and transparency in documenting ships and the crews that work on them. We are

actively discussing with GOP counterparts ways in which we can enhance maritime security through more robust information sharing.

#### Anti-Corruption

14. (SBU) After campaigning on a "zero-corruption" platform, Torrijos launched a number of anti-corruption investigations and initiatives in the opening weeks of his administration, including the formation of an Anti-Corruption Council. The controversy over corruption within the Supreme Court continues to attract popular interest, especially after a recent spate of characteristically egregious rulings. In December 2005, two Supreme Court seats will open up when the 10-year terms expire. In a bid to clean up Panama's politicized Supreme Court, in October 2004 Torrijos replaced the controversial Supreme Court president, Cesar Pereira Burgos, who had passed retirement age.

15. (SBU) At the end of September 2005, a commission that President Torrijos formed in March to make proposals on justice sector reform released its detailed report and recommendations. The Embassy supports that effort, and continues to build its strong Good Governance initiative, which began with the former Ambassador's 2003 speech against official corruption. Her speech resonated firmly with Panamanians from all walks of life and generated front-page headlines. She also stated publicly that poverty could pose dangers for democracy and that skewed income distribution and social injustice increase the appeal of unscrupulous populist demagogues. The Embassy currently supports good governance activities directed toward judicial reform, civic education, business ethics, and strengthening the anti-corruption prosecutors' institutional capacity.

#### Visa Revocations

16. (SBU) An important element of the Embassy's Good Governance initiative is its visa revocation program. Based on Embassy recommendations, the State Department in summer 2004 revoked the U.S. visas of two former senior GOP officials, which provoked a spate of mostly favorable press commentary and huge support (85% according to one poll) from average Panamanians. A third visa, of former Maritime Authority Director Bertilda Garcia, was revoked in early March, 2005. Several other corrupt officials have lost their visas for money laundering or related issues and we are ever alert to ensure that other corrupt officials who have harmed USG interests may not travel to the United States.

#### Macroeconomic Climate

17. (U) Panama's approximately \$14 billion economy is based primarily on a well-developed services sector that accounts for roughly 80% of GDP. Services include the Panama Canal, banking and financial services, legal services, container ports, the Colon Free Zone (CFZ), and flagship registry. Panama also maintains one of the most liberalized trade regimes in the hemisphere. U.S. bilateral trade with Panama came to \$2.1 billion in 2003. U.S. exports were \$1.8 billion and imports were \$301 million in 2003. The stock of U.S. Foreign Direct Investment (FDI) in 2002 was \$20 billion. U.S. FDI is primarily concentrated in the financial sector.

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